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IN THE
Supreme Court of the United States

OCTOBER TERM, 1943

No. 858

SANTLY BROTHERS, INC.,

Petitioner,

against

W. A. WILKIE, sometimes known as BUD WILKIE,

Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO THE
PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE SECOND CIRCUIT

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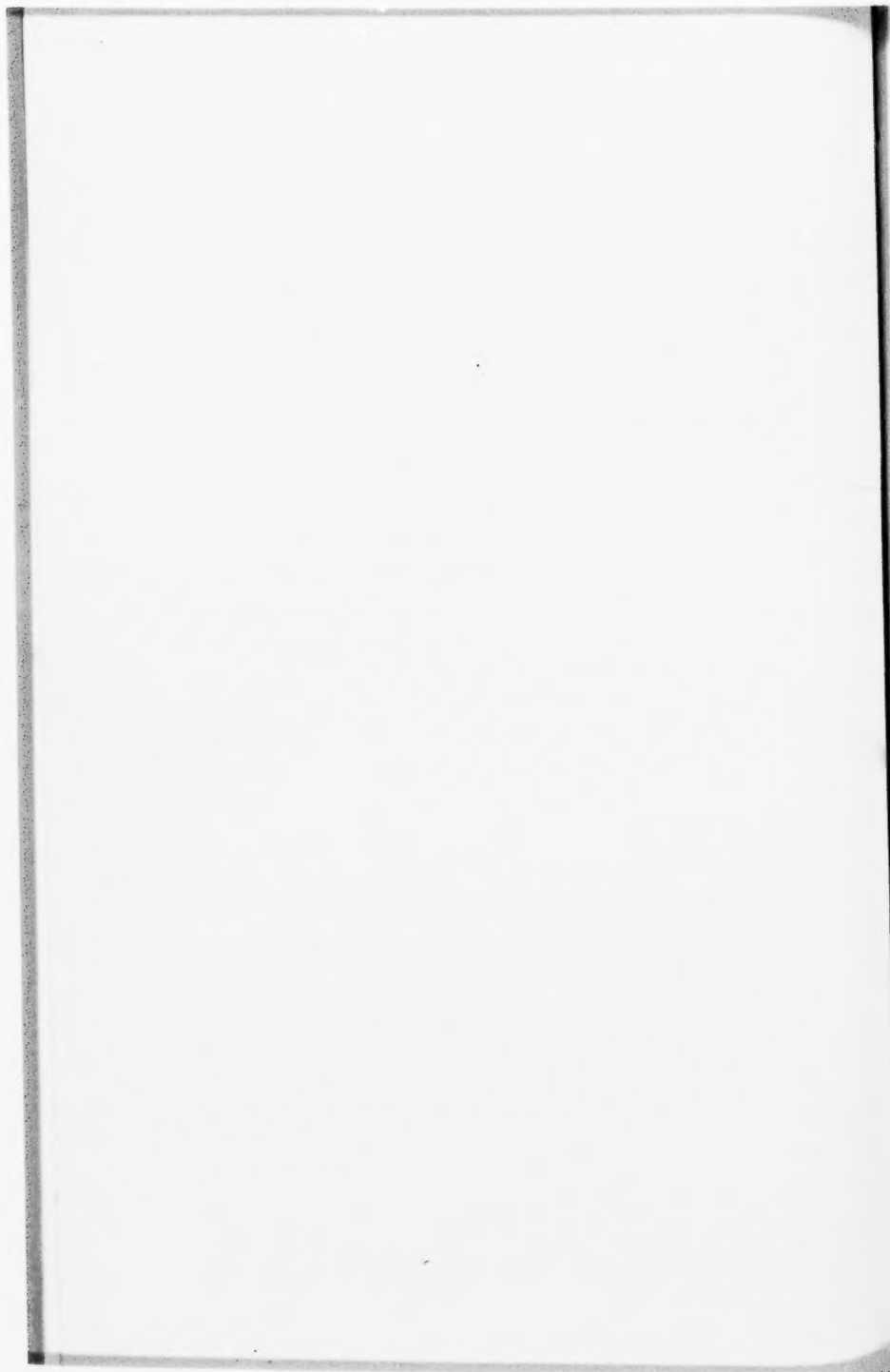


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*To the Honorable the Chief Justice and the Associate
Justices of the Supreme Court of the United States:*

The respondent respectfully prays that the petition for a Writ of Certiorari to the Circuit Court of Appeals for the Second Circuit to review the final judgment of that court entered on January 7, 1944, be denied.

**The Questions Set Forth in the Petition Are Not
Involved in the Instant Case.**

Petitioner attempts to convey the impression that the Master predicated his determination of the profits derived from the infringing song on a speculative appraisal and an artificial separation of inseparable businesses.

The fact is that the Master computed the net profit derived by petitioner from the infringing song by deducting from the gross profit (as set forth in the petitioner's account [R. 13-17] and adjusted with the consent of the

latter [R. 196, Finding 7]), a proportionate share of the overhead expenditures incurred by petitioner in its entire business. The proportion was determined by allocating the overhead expense between the infringing song and the non-infringing songs published and distributed by petitioner during the accounting period (R. 206-208).

There was no issue as to the propriety of segregating the infringing gross profit from the non-infringing gross profits. Nor was there any issue as to the necessity of apportioning the overhead expenses between the infringing and non-infringing activities, for petitioner itself segregated the profits and apportioned the overhead in the account filed by it with the Master (R. 13-17).

The only question submitted to the Master, in addition to the propriety of deducting certain specific items of overhead, was the proper formula for apportionment of the overhead expenses between the infringing and the non-infringing songs.

Respondent contended that all of the overhead should be apportioned on the basis of the number of songs of equal importance published and distributed by petitioner during the accounting period; the petitioner claimed that the apportionment should be on the gross sales basis.

The Master found that the gross sales formula should be applied to that portion of the overhead which had been directly increased by the publication of the infringing song. He held that the numerical formula should be applied to the balance of the overhead which had not been so increased (R. 198, 206-208).

Accordingly, it was solely with reference to the question of apportionment that the Master made the statements as to the necessity of separating the business and of approximating the amount. Petitioner's quotation was incompletely excerpted. The Master's full comment was:

"The next question is on what basis to apportion the overhead between 'Starlight' and the rest of the

business. Santly contends that it should be on the sales basis which would charge 'Starlight' with 13.62%. Plaintiff contends that it should be on the numerical basis, taking forty-seven songs of which Santly sold over fifty copies and disregarding nine of which less than fifty copies were sold. This would charge 'Starlight' with $1/47$ th or 2.13%. No other basis of apportionment has been suggested (R. 206-207) * * *

If the entire overhead should be apportioned on the sales basis of 13.62% to 'Starlight,' the song would show a loss, although by every practical test it was a conspicuous success. * * * Santly's business as a whole was conducted at a loss during the accounting period in spite of the success of 'Starlight,' but plaintiff is entitled to separate the 'Starlight' business from the unprofitable business and recover the 'Starlight' profits. If Santly is permitted to burden the plaintiff with the expenses of the unprofitable business to any extent, to such extent will Santly be permitted to retain 'Starlight' profits. An appraisal of the extent to which the overhead expenditures assisted in the publication and distribution of 'Starlight' is necessarily a speculative appraisal but it must nevertheless be made. It is necessary to speculate and to decide the case on its own facts. Santly was engaged primarily in distribution and most of its overhead was general cost of distribution which would not ordinarily vary with sales. Fast selling articles take less time and effort than slow selling ones" (R. 208).

That an apportionment of overhead must be made and that it must necessarily be approximate and to some extent speculative, was fully recognized by petitioner who made the following statement in the account filed by it with the Master:

"To this item must be added the amount of the apportionment of the general cost of operation for said period, which is difficult of computation * * *"
(R. 15).

Accordingly, petitioner's statement that the Master's finding of a net profit in the sum of \$6,619.65 was based on the theory "that the petitioner's business was to be considered as two separate businesses" is incorrect.

The questions formulated in the petition are based upon the fallacious assumption that the Master created a hypothetical net profit on the infringing song. It has been demonstrated that the net profit was computed by deducting a portion of the overhead expenses from the gross profit on the infringing song. Therefore, the only question is whether the method of apportionment followed by the Master is fair and equitable under the particular circumstances of the case.

This is conclusively demonstrated by the fact that except for an objection to the elimination by the Master of three specific items of overhead, the only contention made by the petitioner in the District Court on respondent's motion to confirm the report, referred solely to the apportionment of overhead expenses. The Court in its opinion said:

"The first question to be considered is whether the Master's treatment of overhead expense is correct. That this is the main issue is recognized by both sides" (R. 231).

The additional argument presented by petitioner for the first time in the Circuit Court that petitioner "derived no profit whatever from the infringement because its business as a whole showed a loss during the infringing period" (R. 251) was obviously a mere amplification of its basic contention that the portion of overhead allocated to the infringing song was insufficient. Accordingly, the Circuit Court too held that "the principal issue is whether in the accounting proper credit was allowed to the publisher for overhead" (R. 251).

There Is No Novel Question of Law Involved in the Instant Case. The Authorities Have Specifically Avoided Statement of Rules of Law in Applying Ratios of Apportionment. Different Formulae Have Been Approved in Different Cases.

The costs of the infringement must be deducted to ascertain the benefits, if any, to the infringer. These costs are in part reflected in increase of overhead expense. To allocate this overhead expense, an approximation must be made. Allocation with mathematical precision is by the nature of the case impossible. Rent and light do not lend themselves to direct division. This practical impossibility of precise allocation has led to the use of many formulae. The courts have recognized that in each instance, the ratio of apportionment has to be intelligently related to the nature of the business and the nature of the infringement.

The difficulties of accounting may prevent any mathematically precise apportionment, but the differences of fact nevertheless require limiting even the rule of thumb formula to that situation where it appears at least to approximate the equities.

It is well settled that the method of apportionment of overhead expenses between the infringing and non-infringing activities, depends upon the particular circumstances of each case and that the method adopted in one case cannot be considered as a statement of a rule of law.

Levin Bros. v. Davis Mfg. Co., 72 F. (2d) 163:

“* * * because a recurring item, like overhead, is handled a certain way in a given case, such is no statement of a rule of law that the same item must be similarly dealt with in all cases. The ‘rules’ contended for by the parties here are not rules of law. They are but illustrations of applications of the above single broad rule to different fact situations.”

Gehring v. Fox Typewriter Co., 251 Fed. 584,
cert. den. 284 U. S. 598:

"It is difficult and often impossible to arrive at an accurate apportionment in a case of this kind, and each case must stand on its own facts. * * * We are not prepared to say that the apportionment adopted by the Master would be applicable in all cases; but, in the state of this record, we think it worked out an equitable result and did substantial justice between the parties."

A. Mecky Co. v. Gaxton Toy Co., 277 Fed. 507,
510:

"Reference is made to overhead. There are few cases in which overhead and its proportional allotment to various lines in a single factory is not entirely a matter of judgment or estimate; and, of course, no matter what the basis of allotment, it is in a sense arbitrary."

The formula of apportionment used by the Master met the equities of the instant situation to the greatest possible extent, since the overhead expenditures apportioned by the Master on the basis of the number of songs of the same class published and distributed by petitioner were not increased by the infringement (R. 206, 207, 208).

The opinion of the Circuit Court expresses in concise and clear language the reasons for upholding in the instant case the method of apportionment adopted by the Master.

"The infringing publication was the largest seller, indeed only three others even approached its sales volume. If the fixed overhead should be apportioned on the basis of copies sold, that proportion would of course vary directly with the number of sales of a particular song; although it was shown that no one song was more responsible for, or its publication more assisted by, this sort of overhead than was another. In the absence of any rule of law requiring the use of such a method in these circum-

stances, the result would be so unfair as to preclude the use of the method.

* * * * *

The method which will best do that in this instance was, we think the one used. The expense of this indirect overhead had to be borne by the appellant whether it published the infringing song or not. As the publication of the latter neither increased it nor decreased it, and the same may be said of each of the other, it was fair to treat it as of equal assistance to the publication of each, since in the aggregate they all required it, and to divide it, accordingly. Surely this fixed overhead was not of more assistance to the publication of the infringing song because the sales of it were (fol. 254) comparatively large. Nor was the part of these expenses played in the publication of the appellant's other songs any less by reason of the smaller demand and consequently smaller sales of them" (R. 252, 253).

The propriety of that formula of apportionment in a similar situation was recognized by the Circuit Court of Appeals for the Second Circuit in *Sheldon, et al. v. Metro-Goldwyn Pictures Corporation, et al.*, 106 F. (2) 45, 51; cert. denied 308 U. S. 617:

"The next question is how to find the proper distribution cost of the infringing picture. Several ways might be theoretically proper; but we have to choose between only two: one, to divide the total by the number of pictures distributed by the defendants in 1932; the other, to divide it by the infringing picture's proportion of the total gross receipts. The master took the first; the defendants wish us to take the second; nobody suggests that the costs should be divided in accordance with the cost of production. The distribution cost is made up of a number of items, some of which it might be better to divide by one rule, and some by another. For example, the cost of the advertisements and other publicity might very well vary with the cost of pro-

duction; the cost of carriage might perhaps best be divided by the number of theatres at which the picture was exhibited. But we cannot see why on any theory the cost of distribution should vary with gross receipts. As between the two we therefore accept the master's disposition of this item."

The Instant Case is in Accord With the Well Established Authorities.

Petitioner contends that there is no precedent for the "creation" of infringing profits by separating the infringing business from the non-infringing business. No artificial profits were "created" in the instant case. The actual profit realized on the infringing song was determined by the Master on the basis of petitioner's account and a proportionate allocation of the entire overhead during the accounting period.

Furthermore, this Court has repeatedly held that profits realized from an infringement cannot be offset by losses incurred or sustained on other transactions.

Duplate Corporation v. Triplex Safety Glass Co., 298 U. S. 448:

"A sale resulting in a loss may not be offset by an infringer against another and independent sale for the purpose of extinguishing or reducing a liability for profits."

Petitioner is in error in contending that the decision of the Circuit Court in the instant case is in conflict

(a) with the prior decision of the same court in *Merrell Soule Co. v. Powdered Milk Co.*, 7 F. (2d) 297;

(b) with the decision of this court in *Rubber Company v. Goodyear*, 9 Wall. 801; and

(c) with the decision of the Circuit Court for the 3rd Circuit in *Macbeth-Evans Glass Co. v. L. E. Smith Glass Co.*, 23 F. (2d) 459.

a. In *Merrell Soule Co. v. Powdered Milk Co.*, the defendant infringed a patent for a process of converting milk into a dry powder. On the accounting, it was found that defendant, instead of buying the milk on the open market, bought a creamery and utilized the skimmed milk produced therein and that the creamery was operated at a loss during the accounting period. Nevertheless, the Master made an award of profits computed on the basis of the cost of the skimmed milk on the open market instead of its actual cost to the defendant.

The Court said:

“This procedure is in our judgment inconsistent with the facts and opposed to the law. As to the facts, there is no satisfying proof that, considering the location of defendant’s creamery, there was any sufficient supply of skim milk available for purchase, while the law is plain that even that trespasser, the infringer, is liable only for ‘actual not possible gains,’ and that there were no actual gains stands admitted. *Rubber Co. v. Goodyear*, 9 Wall. 801, 19 L. Ed. 566; *Coupe v. Royer*, 155 U. S. 565, 15 S. Ct. 199, 39 L. Ed. 263.”

Hence, in the *Merrell Soule Co. v. Powdered Milk Co.* case an attempt was made to award the hypothetical profits which defendant would have made had it conducted its business in a different manner. In the instant case, the profits awarded to the respondent are the actual profits realized from the infringing song.

b. *Rubber Company v. Goodyear*, 9 Wall. 788, was an action for infringement of patent. The Master found that the infringer manufactured articles covered and articles not covered by the patent in question and that no separate account was kept as to their respective cost and profit. The Master apportioned the profits but disallowed certain items of expenses. The defendant ap-

pealed to the Supreme Court from the decree of the Circuit Court confirming the judgment below in favor of the complainant. The excerpt from the opinion of the Supreme Court quoted by petitioner refers solely to the contention made by the appellant that the Master improperly disallowed the deduction of "manufacturer's profits and interest on the capital stock." This clearly appears if the language immediately preceding and following the excerpt quoted is read:

"He refused to allow manufacturer's profits and interest on the capital stock. This was correct. 'The profits made in violation of the rights of the complainants' in this class of cases, within the meaning of the law, are to be computed and ascertained by finding the difference between cost and yield. In estimating the cost, the elements of price of materials, interest, expenses of manufacture and sale, and other necessary expenditures, if there be any, and had debts, are to be taken into the account, and usually nothing else. The calculation is to be made as a manufacturer calculates the profits of his business. 'Profit' is the gain made upon any business or investment, when both the receipts and payments are taken into the account. The rule is founded in reason and justice. It compensates one party and punishes the other. It makes the wrongdoer liable for actual, not possible, gains. The controlling consideration is, that he shall not profit by his wrong. A more favorable rule would offer a premium to dishonesty, and invite to aggression."

This case has no bearing whatsoever on the determination of the case at bar.

c. Macbeth-Evans Glass Co. v. L. E. Smith Glass Co., 23 F. (2d) 459, cited by petitioner as authority in support of its contentions, is in reality, authority for the respondent.

In that case the infringer of a patent for a certain type

of lens claimed that in order to compute profits realized from the infringing article, the cost of the unsold lenses should be added to the cost of lenses sold and the entire profit earned on the sold lenses reduced accordingly. In other words, the contention of the defendant therein was similar to the argument made by petitioner in the instant case that the profit realized by it from the infringing song should be reduced by the losses incurred on the other songs. The Court held that defendant was not entitled to claim a credit for the cost of manufacturing unsold lenses, in reduction of profits derived from lenses sold. Similarly, in the case at bar, it was held that petitioner is not entitled to deduct from the net profits derived from the infringing song, the portion of overhead allocated to the non-infringing songs.

The excerpt from the opinion quoted by petitioner refers to the discussion by the Court of the contention made by the defendant that *Continuous Glass Press Company v. Schmerz Wire Glass Company*, 219 Fed. 199, was authority in support of defendant's claim that the cost of unsold lenses should be deducted from the profit derived from lenses sold. The Court observed that this claim was contrary to prior decisions and that the defendant was relying on an isolated paragraph of the opinion in *Continuous Glass Company*, separated from its context.

The Court said:

"This expression was not intended as a statement of abstract law applicable to all cases, but as a statement of law applicable to that case • • • (p. 461).

When read with the context it is clear that the paragraph refers directly, quite correctly and conclusively to the defendant's infringing practice and its liability on its non-showing" (p. 462).

Thus, it is clear that *Macbeth-Evans Glass Co. v. L. E. Smith Glass Co.* fully supports the decision in the case at bar.

Petitioner contends that *Tilghman v. Proctor*, 125 U. S. 136, *Fox Typewriter Co. v. Underwood Typewriter Co.*, 287 Fed. 447, 452, *Mowry v. Whitney*, 14 Wall. 620, *Brown Bag-Filling Machine Co. v. Drohen*, 171 Fed. 438, cited by the Circuit Court in support of its determination, are distinguishable on the ground that they involve the use of an infringed patented apparatus process or improvement and not the infringement of a regular article of manufacture.

This contention is wholly unsound. The only distinction which has ever been made between the use of infringing patented processes or means and the infringement of articles of manufacture, insofar as the computation of profits is concerned, refers solely to the ascertainment of the gross profit realized by the infringer and has no bearing whatsoever on the apportionment of overhead expenses. Obviously, the gross profit realized from the manufacture of an infringing article is shown by the amount received from the sale thereof; on the other hand, a patented process or apparatus is merely an improvement upon an existing process or apparatus and therefore it is sometimes held that a comparison shall be made between the profits obtained and production costs incurred with and without the infringed improvement.

This distinction was made in *Macbeth-Evans Glass Co. v. L. E. Smith Glass Co.* (23 Fed. 2d 459, 461, 462) as follows:

“It was a suit for infringement of a patent for an apparatus and process of manufacture, not for an article of manufacture. Accordingly, the accounting was not for profits derived from infringing sales but for the infringing use of the patented machine and process. Primarily, the measure of profits derived from an infringing use is in the infringer's gain or saving, which in turn is determined by comparing the cost of production by the infringing use with the cost of production by another machine or process when such exists. This is known in the law

as the 'standard of comparison.' When, as in the Continuous Glass Case, none exists, then the infringer's gain or saving is measured by the profits realized from the sale of the resultant product."

Hence, the distinction between an infringement of articles of manufacture and that of patented processes or means might under certain circumstances be material to ascertain the profit realized from the infringement. It is wholly immaterial to the question of deduction of non-infringing losses. Thus in *Fox Typewriter Co. v. Underwood Typewriter Co.*, 287 Fed. 447, 452, the Court said:

"It is a case in which the *amount of recovery is limited* to so much of the profits received by appellant from the sale of its typewriter with appellee's tabulator attached thereto *as was due to such tabulator*. Appellee is entitled to this profit, *even though appellant's business was a losing venture.*" (Italics ours.)

The decisions of this Court make it perfectly clear that the rule excluding the deduction of non-infringing losses from the infringing profit obtains regardless of whether the infringement was of an article of manufacture or of a process or apparatus:

Tilghman v. Proctor, 125 U. S. 136:

"If the defendant gained an advantage by using the plaintiff's invention, that advantage is the measure of the profits to be accounted for, even if from other causes the business in which that invention was employed by the defendant did not result in profits."

Crosby Steam Co. v. Consolidated Safety Co.,
141 U. S. 441, 457:

"The only subject of inquiry is the profit made by the defendant on the articles which it sold at a profit and for which it received payment."

Duplate Corporation v. Triplex Safety Glass Co., 298 U. S. 448:

"A sale resulting in a loss may not be offset by an infringer against another and independent sale resulting in a gain for the purpose of extinguishing or reducing a liability for profits * * * Upon a statement of an account, a patentee is not looked upon as a 'quasi-partner of the infringers,' under a duty to contribute to the cost of the infringing business as a whole."

The facts in the instant case dramatically reveal the correctness of this rule, for the Master found that the infringing song "by every practical test (it) was a conspicuous success," but the petitioner, by means of its improper apportionment of overhead, established a loss. The petitioner contended for a rule which would permit the converted property to fall back into his possession while he placed an empty hand to the respondent. The Master correctly pointed out that according to the petitioner's theory "if Starlight had been twice as successful, it would still show a loss because the increase in percentage of overhead would keep pace with the increase in receipts" (R. 208).

WHEREFORE, it is respectfully submitted that the petition raises no question of law which could justify the granting of a Writ of Certiorari and should therefore be denied.

Respectfully submitted,

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